

Jensen LBOs

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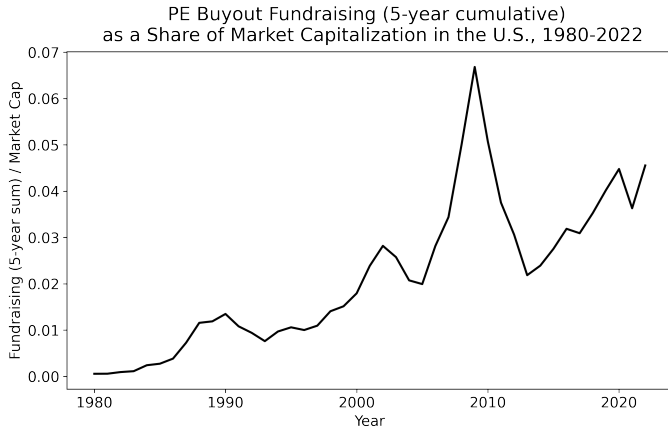
Tim Jenkinson, University of Oxford

Stefan Weik, University of St.Gallen

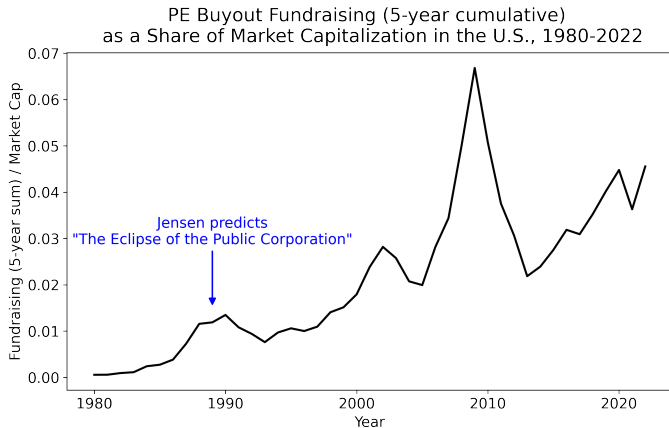
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PE Buyouts expanded a lot since their birth in 1980s



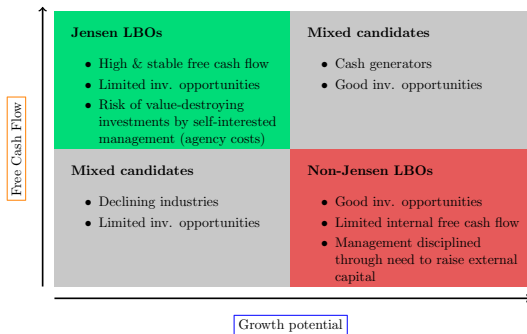
PE Buyouts expanded a lot since their birth in 1980s



- Due to PE leverage, data incompleteness, co-investments, real share is (much) higher.
- So, was Jensen right in predicting "The eclipse of the public corporation" (1989)?

Jensen's LBO Theory (1989) argues PE is superior only in *some* situations—when agency costs are high

"The public corporation is not suitable in industries where long-term growth is slow, where internally generated funds outstrip investment opportunities [...]"



This paper

1. **Testing Jensen's Theory, we find: Jensen LBOs (low-growth, high cashflow) consistently outperform**
 - Utilizing 14,000+ deals over 4 decades to analyze cross-section
 - Persistent outperformance over decades (and robust to different ways of operationalizing Jensen LBOs)
2. **Governance seems to be the mechanism**
 - Driven by primary LBOs (when PE governance is new), muted in secondaries
 - More governance activism: CEOs are 23% more likely to be replaced in Jensen LBOs
3. **However, the prevalence of Jensen LBOs decreased**
 - In 1980s, 90% of deals were in high-agency cost situations, today 50%
 - Might be one driver of the private and public equity return convergence

Overview of the Talk

- ① Data
- ② Main Result
- ③ Mechanism
- ④ Decreased Prevalence of Jensen-LBOs
- ⑤ Conclusion

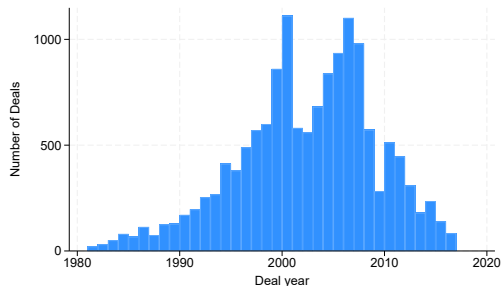
Dataset

Munich Dataset (MDS)

- 14,430 global LBOs (1981–2017)
- Proprietary deal-level database
- Information includes deal cash-flows (NAV if unrealized), GP, fund, and portfolio company information
- Detailed portfolio company information complemented from public datasets (CapIQ, Pitchbook, Preqin)
- Most recent update currently ongoing (Soon, 1981-2025)

Source: Braun et al. (2017, 2020, 2023)

Distribution over Time



Key advantage of our data: very comprehensive in early days (for 2010s, we currently work on extension)

Table: Global Buyout Deal Count

Year	Databases			Coverage	
	Capital IQ (CIQ)	Pitchbook (PB)	Munich Dataset (MDS)	PB as % of CIQ	MDS as % of CIQ
1980-89	820	667	689	81%	84%
1990-99	7,355	5,386	4,196	73%	57%
2000-09	42,050	31,781	7,641	76%	18%
2010-17	48,737	54,849	1,904	113%	4%
Total	98,962	92,683	14,430	94%	15%

Agency Cost Proxies

1. Low-growth

- Tobin's $Q = EnterpriseValue(EV)/TotalAssets(TA)$
- Low Q (< 1) indicates “overinvestment”, with agency cost potential

2. Free Cash Flow

- $FCF = (NetOperatingCF - Capex)/EV$
- Proxy for agency costs of free cash flow

- Problem: valuation and accounting info are mostly not available for private companies
- Solution: we use **industry aggregates** from public markets as proxies

Linking Deals to Industry-Aggregate Agency Proxies

3-Steps:

1. Granular Industry Classification

- Collect 4-digit SIC codes for deals from CapitalIQ, Pitchbook, Preqin, Orbis
- For missing SIC codes: Use GPT-4 based on business descriptions » Validation
- Map SIC to Fama-French 49 industries

2. Compute industry-country-year level Agency Proxies

- Based public market data from Worldscope: 75.000+ listed firms

3. Link Deals to Aggregates

- On industry-country-year(-1), December prior to deal year (avoid look-ahead bias)

Country_Industry_Year	Public company universe		Private equity LBO deals	
	Obs.	Tobin's Q median	Obs.	Jensen LBO? (Industry $Q < 1$)
USA_SOFTW_2000	514	2.07	117	Non-Jensen LBO
USA_WHLST_2000	214	0.79	19	Jensen LBO

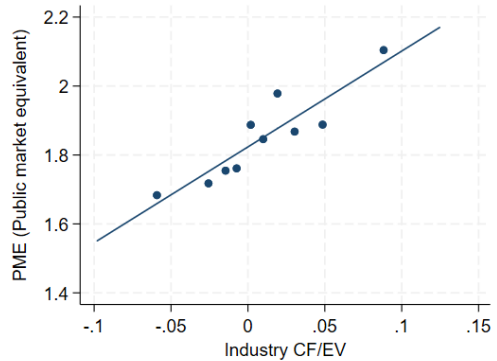
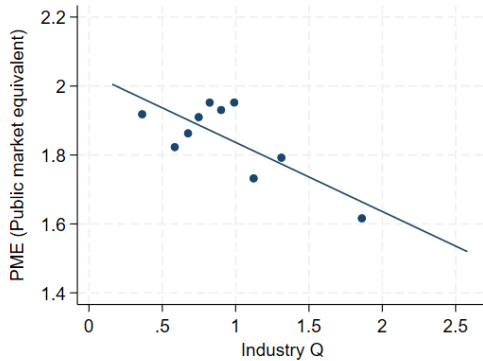


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Main result: Jensen-LBOs (low growth, high cash-flow) outperform

Panel B: PME



Main Result: Jensen-LBOs (low growth, high cash-flow) outperform - descriptive

Cash-flow to EV	Tobin's Q		Low - High Q
	Low	High	
Panel A: MOIC			
High	2.58	2.50	0.08
Low	2.34	2.04	0.30***
High - Low	0.24***	0.46***	
Panel B: PME			
High	1.96	1.87	0.09*
Low	1.80	1.65	0.15***
High - Low	0.16***	0.22***	

Main Result: Jensen-LBOs (low growth, high cash-flow) outperform - regression

Dependent variable	PME							
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Industry Q	-0.13*** (0.04)	-0.11** (0.05)						
Industry $Q < 1$ (0/1)			0.11*** (0.04)	0.09** (0.04)				
Industry cash-flow to EV					2.05*** (0.47)	1.72*** (0.48)		
Industry cash-flow to EV > 0 (0/1)							0.14*** (0.04)	0.12*** (0.04)
Observations	14429	14426	14429	14426	14429	14426	14429	14426
R-squared	0.05	0.09	0.05	0.09	0.05	0.09	0.05	0.09
Region-Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
GP FE	No	Yes	No	Yes	No	Yes	No	Yes
Average dependent var	1.85	1.85	1.85	1.85	1.85	1.85	1.85	1.85

All specifications control for deal size and fund age. Industry is Fama-French 49. Industry variables equal the median of all public firms in the same industry, country, and year as the target company as of December prior to the deal year.

Jensen-LBOs with consistent outperformance over time

Dependent variable:	PME							
Sample:	Early years (1981–2000)				Late years (2001–2017)			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Industry Q	-0.21** (0.08)				-0.15** (0.07)			
Industry Q < 1 (0/1)		0.17** (0.07)				0.06 (0.06)		
Industry cash-flow to EV			2.47*** (0.84)				2.47*** (0.81)	
Industry cash-flow to EV > 0 (0/1)				0.32*** (0.07)				0.10* (0.06)
Observations	6341	6341	6341	6341	4782	4782	4782	4782
R-squared	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04
Region-Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
GP FE	No	No	No	No	No	No	No	No
Average dependent var	2.05	2.05	2.05	2.05	2.01	2.01	2.01	2.01

- Here, we filter for realized deals, to leave later deals time to be realized.
- Further investigation needed when more recent deal data update is completed to test whether decreased relevance of binary proxies means decreased relevance of agency costs or industries drifting away from theoretical thresholds.

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Mechanism

Governance hypothesis: PE governance drives Jensen-LBO outperformance.

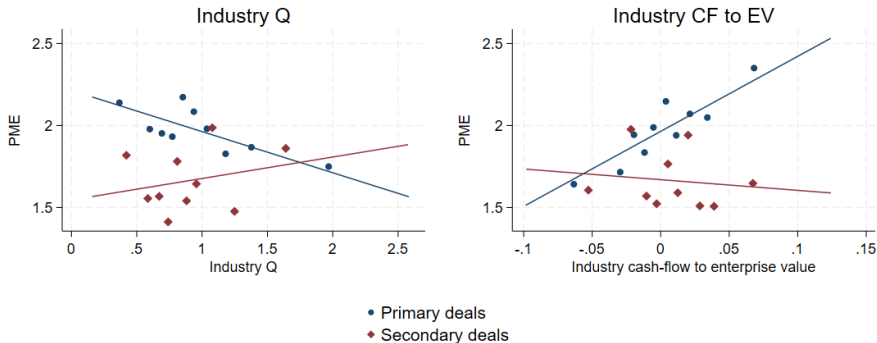
Test 1: Governance Headroom (Primary vs. Secondary LBOs)

- Primary LBOs should have higher agency costs that can be resolved than secondaries, which were PE-owned before.
- **Prediction:** Jensen LBO-performance relationship stronger in primary LBOs; muted in secondaries.

Test 2: Governance Actions (CEO Turnover)

- PEs list management change as main source of value creation (Gompers et al., 2016)
- **Prediction:** We should expect more governance action (e.g., CEO turnover) in Jensen LBOs.

Test 1: Jensen-LBO outperform only in primary LBOs

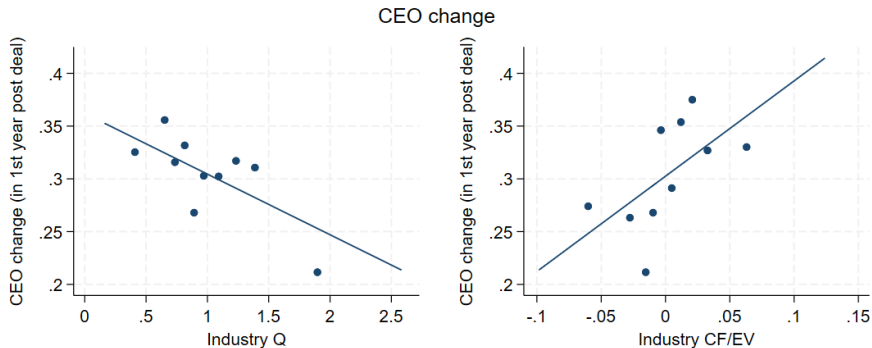


- High-agency-cost deals only outperform if they are PE-owned for the **first time**.
- Relationship muted in secondary LBOs.

Test 1: Jensen-LBO outperform only in primary LBOs

Dependent variable:	PME							
Sample:	Primary LBOs				Secondary LBOs			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Industry Q	-0.22*** (0.06)				0.30* (0.17)			
Industry Q < 1 (0/1)		0.19*** (0.06)				-0.27*** (0.10)		
Industry cash-flow to EV			3.53*** (0.70)				-0.15 (1.19)	
Industry cash-flow to EV > 0 (0/1)				0.21*** (0.05)				-0.00 (0.08)
Observations	7411	7411	7411	7411	1453	1453	1453	1453
R-squared	0.04	0.04	0.04	0.04	0.11	0.11	0.11	0.11
Region-Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
GP FE	No	No	No	No	No	No	No	No
Average dependent var	1.97	1.97	1.97	1.97	1.66	1.66	1.66	1.66

Test 2: Jensen-LBOs predict Governance Actions



- CEO change is more likely in high-cashflow and low-growth situations – consistent with higher agency costs.

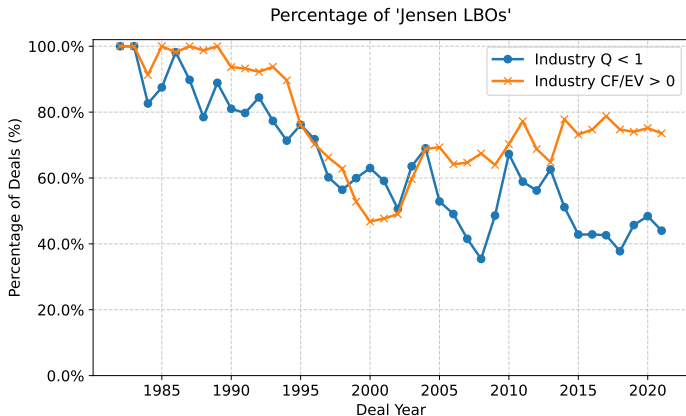
Test 2: Jensen-LBOs predict Governance Actions

Dependent variable:	CEO change in 1st year post-deal							
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Industry Q	-0.06** (0.03)	-0.06** (0.03)						
Industry Q < 1 (0/1)			0.04 (0.02)	0.03 (0.03)				
Industry cash-flow to EV					0.97*** (0.32)	0.99*** (0.34)		
Industry cash-flow to EV > 0 (0/1)							0.07*** (0.02)	0.06** (0.02)
Observations	2073	2045	2073	2045	2073	2045	2073	2045
R-squared	0.03	0.12	0.03	0.12	0.03	0.12	0.03	0.12
Region-Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
GP FE	No	Yes	No	Yes	No	Yes	No	Yes
Average dependent var	0.31	0.31	0.31	0.31	0.31	0.31	0.31	0.31

Overview of the Talk

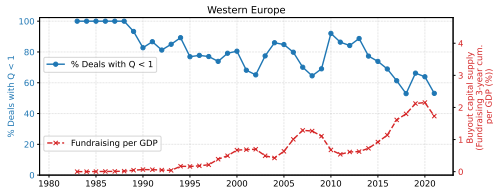
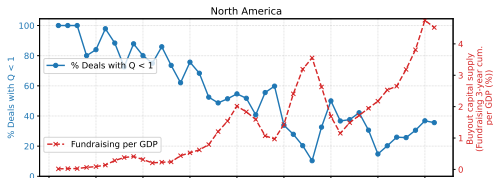
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Jensen LBOs are less prevalent over time

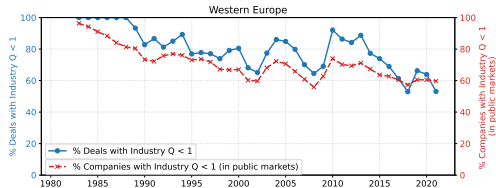
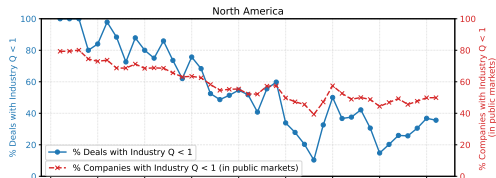


"Demand" and "Supply" for Jensen-LBOs

"Demand" (Buyout funds raised)



Supply (Available companies)



Demand and supply explain most of the variation in Jensen-LBO share

Dependent variable:	% of 'Jensen LBOs' (with Industry $Q < 1$)			
	(1)	(2)	(3)	(4)
Buyout competition (Fundraising 3-year-cum. / GDP %)	-24.83*** (1.89)	-10.17*** (2.37)	-9.78*** (2.78)	-8.32*** (2.73)
% of companies with $Q < 1$ (in public market)		140.25*** (20.99)	146.56*** (23.91)	165.52*** (22.35)
Decade FE	No	No	Yes	No
Region FE	No	No	Yes	No
Region-Decade FE	No	No	No	Yes
Observations	128	128	128	128
R-squared	0.668	0.807	0.819	0.847

- For this analysis, we switch to the region-year level
- Buyout competition alone explains 67% of the variation
- Suggests there is limited supply of Jensen-deals available, which could explain why GPs invest in (predictably worse) Non-Jensen deals

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Conclusions and Outlook

Key Findings:

1. Jensen LBOs persistently outperform by 0.07–0.13 PME
 - Not from risk or industry selection, likely PE governance
2. Jensen deal share declined: 90% (1980s) → 50% (today)

Implications:

- Newer research shows that cross-section of deals is relevant to understand PE performance (Stafford, 2022; Volckmann, 2025)
- We provide a theory-motivated framework to explain cross-section of LBOs

Outlook:

- Extend data to recent decade (ongoing)
- Test for causal role of capital supply via exogenous shocks (e.g., pension regulations)

Appendix

AI-generated SIC Codes

Example			Type	Share
Business description	DB SIC	AI SIC		
Manufacturer of transformers intended for utilities, grid operators, [...].	3612	3612	Identical	70%
Provider of radioactive-waste disposal services. The company offers offsite waste processing, disposal [...]	4953 [Hazardous waste mgmt] 7363 [Services-help supply]	4953 [Hazardous waste mgmt]	AI selects one of many	19%
Provider of telecom management services. The company provides management services [...]	4899 [Communications services]	7389 [Business Services]	Disagreement	11%